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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1940.

No. 412

THE FIRST NATIONAL BANK OF CHICAGO, EDGAR STANTON AND JOSEPH C. BELDEN, TRUSTEES FOR THE REW TRUST, TRANSFEREES,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

HERBERT POPE,
FRANCIS H. URIELL,
BENJAMIN M. PRICE,
Counsel for Petitioners.

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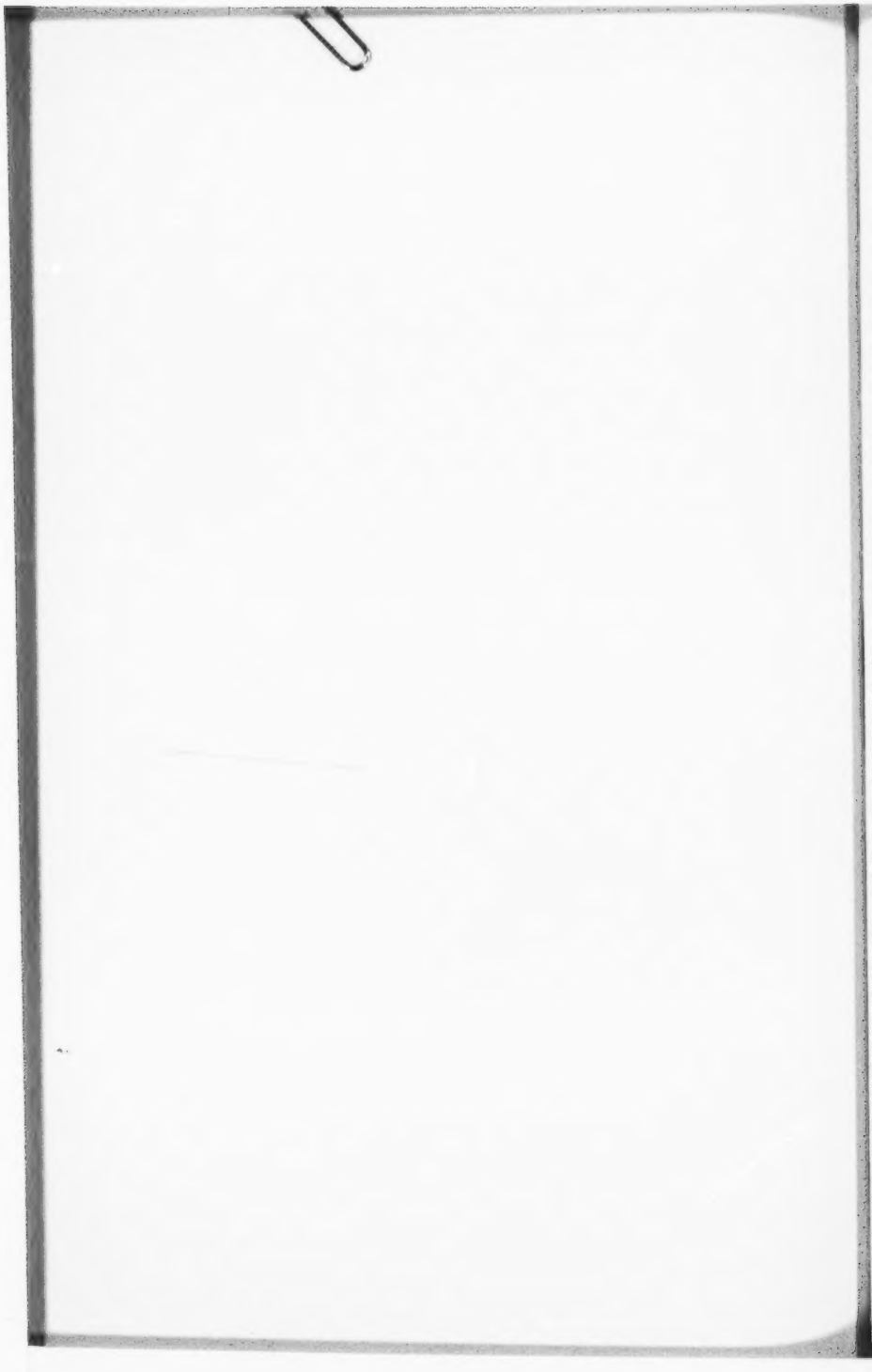

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To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioners, who are the trustees of the Rew Trust, a trust created by George Campbell Rew, now deceased, respectfully pray for the allowance of a writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit to review the judgment of that court entered in the above case on May 13, 1940.

Summary Statement of Matter Involved.

This petition is for review of a judgment of the United States Circuit Court of Appeals for the Seventh Circuit (R. 101) which affirmed a decision of the United States Board of Tax Appeals determining a liability of petitioners, as transferees of George Campbell Rew, deceased, for income taxes alleged to be due by him for the period January 1, 1924, to June 10, 1924, in the amount of $75,478.47 (R. 80).

Nearly thirteen years after Rew's death in June, 1924, a notice of transferee liability was sent to First National Bank of Chicago, Trustee for the Rew Trust, as a transferee of Rew in his lifetime, and one of the principal questions raised before the Board of Tax Appeals and the Circuit Court of Appeals was whether the statute of limitations had barred any assessment against petitioners, as transferees, for a tax liability alleged to have been incurred by Rew before his death. It was conceded that such assessment was barred in 1929 by the provisions of Section 280(b) and (c) of the Revenue Act of 1926, (Appendix, p. 28), unless the running of the period of limitations provided for in that section was suspended under Section 277(b) (Appendix, p. 27), by a futile proceeding against Rew's executors, who were known to possess no assets beyond what was required to pay taxes and expenses, on the theory that such a proceeding was a proceeding against Rew, the taxpayer. This theory was sustained by the Court of Appeals, that Court holding that the executors, upon their qualification, became Rew, the taxpayer, and the transferor of property in fact transferred by the decedent in his lifetime. This conclusion is based upon Section 281(a) of the Revenue Act of 1926 which the Court of Appeals interprets as meaning that "the executors, upon qualification, so far as liability

of Rew for income tax was concerned, assumed the power, rights, duties and privileges of the taxpayer." (R. 96.) The Court of Appeals ignores the fact that this section of the Revenue Act was not enacted until nearly two years after Rew's death and after his executors had qualified, that the notice required by that section was never given at any time, and that its decision is therefore in direct conflict with the facts and also with a decision of the Second Circuit Court of Appeals to which we will refer. Section 281(a) does not purport to make an executor responsible for all the acts done by the decedent, or for property which the executor did not and could not receive. (Appendix, p. 28.)

Furthermore, this section, which, if applicable, changed the case from one governed by the local law of Illinois to a case governed by a federal statute, was mentioned for the first time by counsel for respondent at the oral argument in the Circuit Court of Appeals and was not asserted before the Board of Tax Appeals or mentioned in the Board's decision. A petition for rehearing (R. 105) called this to the attention of the Court, as well as the fact that in other respects the decision was in conflict with the decisions of all common law courts, including decisions of this Court and of the Supreme Court of Illinois. The petition was nevertheless denied on June 11, 1940.

The Circuit Court of Appeals also held that the decision against the executors was *res judicata* in this proceeding involving transferees of the decedent, although this Court and the Supreme Court of Illinois have both held that a decision against an executor is confined to the property received and held by the executor.

The Circuit Court of Appeals did not consider whether under the decisions of this Court no taxable gain was realized by the taxpayer, the decedent Rew, on an exchange of securities because he was under obligation not

to sell or pledge the securities agreed to be received within six months after he received them. And it did not consider other questions involving the liability of the taxpayer because of its decision on the question of *res judicata*. So far as this petition is concerned the primary question is the suspension of the running of the statute of limitations. The plea of *res judicata* depends upon the same novel theory of the identity of a decedent and his executors with reference to property which the executor did not and had no right to receive.

The transaction here involved occurred nearly seventeen years ago. On December 31, 1923, George Campbell Rew entered into a contract with Peabody, Houghteling & Company, an investment firm, whereby he agreed to deliver and did deliver to Peabody, Houghteling & Company certain preferred stock owned by him in exchange for an agreement to deliver to him certain unlisted bonds which were later delivered to him (R. 23-24). The contract, among other things, provided that Rew could not sell, directly or indirectly, or pledge the securities received by him for a period of six months from the date of the contract (R. 11, 24, 25, 26). The securities received in compliance with that agreement by Rew were miscellaneous unlisted bonds comprising 30 issues (R. 12, 13, 14). Even if Rew had been permitted by his contract to sell these bonds, there was no market whatever for most of them. He could have sold at a discount, had he been permitted to sell by his contract, his small holdings of three issues, but could not have sold the rest of his holdings, except very limited amounts of seven issues, and those he would have had to sell at considerably less than their fair value. (R. 28, 34 to 39, 46).

Rew died on June 10, 1924. Shortly thereafter his will was probated in the Probate Court of Cook County, Illinois, and Edgar Stanton and Joseph C. Belden were

duly appointed as executors of his estate (R. 19). On or about October 8, 1924, the executors, in compliance with section 225 of the Revenue Act of 1924 and the regulations thereunder, filed a federal income tax return on behalf of the decedent for the period from January 1, 1924, to June 10, 1924, with the Collector of Internal Revenue at Chicago, Illinois (R. 19). Thereafter, the Commissioner of Internal Revenue audited said return and claimed that Rew, by virtue of the exchange made by him, pursuant to the contract of December 31, 1923, realized taxable income subject to tax in the amount of $75,478.47, which had not been reported in the return (R. 9). A notice of deficiency was sent to the executors of Rew's will on September 11, 1928 (R. 20).

The executors appealed to the Board of Tax Appeals from such notice of deficiency, claiming that Rew was not taxable, under the provisions of section 202 of the Revenue Act of 1921 relating to exchanges of property for property not having a "readily realizable market value" —a concept that was not carried over into the 1924 Revenue Act, the provisions of which are involved in this proceeding. They claimed that the exchange occurred in 1923 and that likewise any income attributable thereto accrued in 1923. On June 5, 1936, the Board rendered a decision adverse to the executors (34 B. T. A. 451). The Circuit Court of Appeals affirmed the Board's decision on July 28, 1938, *Stanton* v. *Commissioner*, 98 F. (2d) 739. A petition for certiorari was denied by this Court on December 5, 1938 (305 U. S. 650).

Before his death Rew had created two trusts. One dated December 31, 1923, was designated "The George Campbell Rew Trust" and in it he transferred to the trustees therein named certain securities. Among the securities embraced in the trust were all of the securities acquired by him in the transaction that was the subject

matter of the litigation described in the proceedings against the executors (R. 75). On March 10, 1924, Rew created another trust designated "The Rew Trust" and transferred to himself as trustee thereof substantially all his remaining assets (R. 19). It is this latter trust which the petitioners as trustees represent in this proceeding. In this trust the decedent reserved to himself for life the income from the trust, and also retained an unlimited power of revocation.

On June 23, 1937, approximately 13 years after Rew's death, a notice of transferee liability was sent to First National Bank of Chicago, trustee for The Rew Trust, as transferee of the assets of the decedent, proposing to assess a transferee liability of $75,478.47 plus interest against The Rew Trust as transferee. These petitioners as trustees of The Rew Trust filed a timely appeal to the Board of Tax Appeals from such notice of liability (R. 1, 7).

Before the Board these petitioners claimed that the statute of limitations barred the assessment against them of any tax liability of Rew; that by reason of the restriction contained in the contract of December 31, 1923, under which Rew received the securities from Peabody, Houghteling & Company, the "fair market value" of the securities received by him could not be ascertained with certainty sufficient to satisfy the requirement of the Revenue Act of 1924; that if there was a taxable gain it was realized in 1923, not in 1924, the year here involved; and that they were not liable as transferees of a revocable trust. The Commissioner took issue with the claim relative to the statute of limitations and pleaded that the proceeding between the Commissioner and the executors was *res judicata* of the tax liability and precluded a contest on the merits of the tax by these petitioners.

The Board, and the Circuit Court of Appeals upon ap-

peal from the Board's decision, decided against the petitioners by holding that the proceedings between the Commissioner and the executors suspended the running of the statute of limitations for assessment against these petitioners and that the judgment against the executors was *res judicata* and precluded these petitioners from contesting the validity of the tax.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on May 13, 1940 (R. 101). A petition for rehearing was subsequently filed and was denied by that Court on June 11, 1940 (R. 113). The jurisdiction of this Court is invoked under section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

Questions Presented.

1. Whether Section 281 (a) of the Revenue Act of 1926 applies in this case when it was not enacted until after the death of Rew and after the qualification of his executors.

2. Whether the Court of Appeals was justified in basing its decision upon Section 281 (a) when the applicability of that provision was not mentioned until the oral argument in that Court and was not presented to or considered by the Board of Tax Appeals.

3. Whether the Court of Appeals, by reason of Section 281 (a), was justified in holding that the executors of Rew's estate, upon their qualification, became the taxpayer in the place of the decedent and the transferor of property transferred in fact by the decedent.

4. Whether the Court of Appeals was justified in holding that this proceeding was not barred by the statute of

limitations by reason of Section 281 (a) or for any other reason.

5. Whether the Court of Appeals was justified in holding that the judgment in the prior proceeding against Rew's executors was *res judicata* by reason of Section 281 (a) or for any other reason.

6. Whether the Court of Appeals erred in failing to hold that the sales restrictions in the contract of December 31, 1923, under which Rew received the securities from Peabody, Houghteling & Co. deprived the securities of an ascertainable fair market value sufficient to support an income tax upon their receipt.

7. Whether the Court of Appeals erred in failing to remand the case to the Board with directions to find facts showing whether the sale of securities occurred in 1923 or 1924.

8. Whether the Court of Appeals erred in holding that the petitioners became transferees who were liable for the alleged income tax liability of Rew.

Reasons Relied on for Allowance of the Writ.

In two respects the decision of the Circuit Court of Appeals is in direct conflict with decisions of Circuit Courts of Appeal of other circuits. It is also in conflict with decisions of the Supreme Court of Illinois, which should govern, and with decisions of this Court which state the law of the country on the effect of judgments against an executor.

1. As to the application of Section 281 (a) of the Revenue Act of 1926, the decision is in direct conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Liberman's Committee* v. *Commissioner*, 54 F. (2d) 527. In both cases the transaction in question took place before that provision of the Revenue Act was

enacted. The Second Circuit held that in such a case the provision could have no application. In this case the Court of Appeals gave the provision controlling effect.

The Court of Appeals, instead of basing its decision upon the local law governing the relation of an executor to the decedent and to other persons receiving other property from the decedent, based its decision upon the ground that "the theory of income taxation" had made the executors in this case "for the purpose of determination, the transferor himself." (R. 98.)

The Court of Appeals avoids the decisions of the Supreme Court of Illinois and of this Court, which are to the contrary, by not mentioning them at all and rests its decision upon the income tax acts. The only income tax provision referred to which is supposed to accomplish this revolution in the law is Section 281 (a) of the Revenue Act of 1926. As to this section the Court of Appeals says (R. 96):

> "Under Section 281 (a) the executors, upon qualification, so far as liability of Rew for income tax was concerned, assumed the power, rights, duties and privileges of the taxpayer."

When the executors qualified Section 281 (a) had not been enacted, and they had in fact filed the tax return which started the running of the statute of limitations in favor of petitioners, long before that section was enacted. No statutory provision is referred to by the Court of Appeals which prevented the Commissioner from proceeding at any time against petitioners. The suspension of the statute is based entirely upon the conclusion that Section 281 (a) made the executors the taxpayer in place of the decedent and the transferor of property which the decedent himself transferred to petitioners.

This conclusion is in direct conflict with the statement of this Court in *Hartley* v. *Commissioner,* 295 U. S. 216,

218, that "The revenue acts consistently treat the estate of a decedent in the hands of an administrator or executor as a separate taxpayer." It is that personal estate alone with which executors are concerned, and therefore a judgment against an executor does not affect an heir, and, as this Court said in *Ingle* v. *Jones*, 9 Wall. 486, 495, "the statute of limitations may be pleaded with the same effect as if there had been no prior recovery against the personal representative." That was the law at least prior to the passage of Section 281 (a), and the transactions in this case occurred before that.

It appears also that the question of the application of Section 281 (a) was mentioned for the first time by counsel for respondent at the oral argument in the Circuit Court of Appeals and was not asserted before the Board of Tax Appeals or mentioned in its decision. The notice required by that section was of course not given because the statute was not in existence when such a notice should have been given. The decision of the Court of Appeals therefore was based upon an assumption contrary to the record and involved a claim not made in the proceeding before the Board and is in conflict with decisions of this Court. It concerned an entirely new case, based upon a federal statute instead of the local law of Illinois.

General Utilities & Operating Co. v. *Helvering*, 296 U. S. 200.

Helvering v. *Tex-Penn Oil Co.*, 300 U. S. 481, 498.

Helvering v. *Wood*, 309 U. S. 344, 349.

2. The decision of the Circuit Court of Appeals is in conflict also with the decision of the Circuit Court of Appeals for the Ninth Circuit in *Commissioner* v. *Krug*, 78 F. (2d) 57, in which a proceeding against one transferee of a taxpayer was held not to suspend the running of the statute of limitations against another transferee. If an

executor is confined to the personal estate which comes into his hands for transfer he is in no different position from another transferee of the decedent. A judgment against the executor can affect only the property which he receives. It is also expressly held by the Supreme Court of Illinois, as we shall show, that an executor has nothing to do with property claimed to have been fraudulently transferred by the decedent. Only creditors of the decedent can reach such property, and they can proceed against executors and transferees at the same time. A judgment against an executor, therefore, could not suspend the running of the statute of limitations in favor of a transferee any more than could a judgment against another transferee of the taxpayer, as was held in the *Krug* case.

Section 281(a) relates to all fiduciaries. There is no separate provision about executors and administrators. A judgment against an executor is in the same position as a judgment against another fiduciary who may receive property from the decedent. Under the decision in the *Krug* case, therefore, a judgment against one transferee trustee would not suspend the period of the statute of limitations in the case of another transferee trustee. Section 281(a) places an executor in the same position as any other fiduciary. If no executor had been appointed in this case the position of the petitioners would be just the same.

3. The Court of Appeals finds Section 281 (a) a reason for disregarding the express language of Subsection 280 (c) of the Revenue Act which fixes the period of the statute of limitations in the case of the death of a taxpayer. That section provides that "the period of limitation for assessment against the taxpayer shall be the period that would be in effect had the death * * * not occurred." The decedent is not only designated as the taxpayer in this provision but the period of limitation is to

be determined as to transferees and others in the same way that it would be if the taxpayer had not died. There is no provision to the effect that if executors are appointed they shall become the taxpayer in place of the decedent as to all property owned at any time by the decedent. Unless Subsection 280 (c) is completely ignored the statutory period in this case expired in 1929, eight years before the proposed assessment against petitioners.

In spite of the language of Subsection 280 (c), the Court of Appeals holds that executors when appointed became the decedent taxpayer and became the transferors of property in fact transferred by the decedent. We contend Section 281 (a) was not intended to modify Subsection 280 (c) or to overrule the law of the land in such violent fashion. Instead of applying Subsection 280 (c) according to its terms, as if death had not occurred, the Court of Appeals interprets the statute as recognizing that Rew did die and as providing that his executors became Rew and did all the things that Rew did.

4. The decision and the opinion of the Court of Appeals, if sustained and followed, would work a revolution in the administration of estates throughout the country. It is contrary to the settled law governing executors and administrators and their relation to the decedent and to other persons receiving property from a decedent. No authority has been cited which supports the Court's revolutionary conclusion, and it is in conflict with decisions of other Circuit Courts of Appeal as well as controlling decisions of the Supreme Court of Illinois and of this Court.

Sanborn v. *Helvering*, 108 Fed. (2d) 311, relied upon by the Court of Appeals, has no application. The tax period in question was the year 1929 and the decedent died in 1928. The executrix, and not the decedent, was the tax-

payer, and the property involved was the property in the estate which was transferred to a legatee.

For these reasons we submit that the decision in this case should be reviewed.

Wherefore, the petitioners respectfully pray that this petition for a writ of certiorari be granted and that the said judgment of the Circuit Court of Appeals for the Seventh Circuit be reviewed by this Court.

THE FIRST NATIONAL BANK OF CHICAGO,
EDGAR STANTON and JOSEPH C. BELDEN,
Trustees for the Rew Trust,
HERBERT POPE,
FRANCIS H. URIELL,
BENJAMIN M. PRICE,
Counsel for Petitioners.